

Internal Revenue Service

Number: **201228025**
Release Date: 7/13/2012

Index Number: 1362.04-00

Department of the Treasury
Washington, DC 20224

Third Party Communication: None
Date of Communication: Not Applicable
Person To Contact:

, ID No.
Telephone Number:

Refer Reply To:
CC:PSI:B01
PLR-146403-11
Date
April 10, 2012

LEGEND

X =

Y =

Z =

State =

Date 1 =

Date 2 =

Date 3 =

Date 4 =

Year =

n =

Dear . :

This letter responds to a letter dated November 3, 2011, submitted on behalf of X by its authorized representative, requesting relief under § 1362(f) of the Internal Revenue Code.

FACTS

The information submitted states that X was incorporated under the laws of State on Date 1. X elected to be an S corporation effective the same date.

On Date 2, X issued shares of stock to Y, a partnership for federal tax purposes, and Z, a corporation for federal tax purposes. In year, X redeemed the stock held by Y. Later, a third party interested in acquiring X concluded that X's S corporation status terminated as a result of X's issuance of stock to Y and Z. On Date 3, X cancelled the shares it had issued to Z and issued replacement shares to the principals of Z. During the period that Z held the stock, both Z and X filed their federal income tax returns consistent with Z being treated as a shareholder of X.

X represents that the circumstances resulting in the termination of X's S corporation election were inadvertent and were not motivated by tax avoidance or retroactive tax planning. X and its shareholders agree to make any adjustments required by the Secretary consistent with the treatment of X as an S corporation.

LAW

Section 1361(a)(1) defines an "S corporation" as a small business corporation for which an election under § 1362(a) is in effect for such year.

Section 1361(b)(1)(B) provides that a small business corporation cannot have as a shareholder a person (other than an estate, a trust described in § 1361(c)(2), or an organization described in § 1361(c)(6)) who is not an individual.

Section 1362(d)(2)(A) provides that an election under § 1362(a) shall be terminated whenever (at any time on or after the first day of the taxable year for which the corporation is an S corporation) the corporation ceases to be a small business corporation. The termination is effective on and after the day of cessation. § 1362(d)(2)(B).

Section 1362(f) provides that if (1) an election under § 1362(a) by any corporation (A) was not effective for the taxable year for which made (determined without regard to § 1362(b)) by reason of a failure to meet the requirements of § 1361(b) or to obtain shareholder consent, or (B) was terminated under § 1362(d)(2) or (3), (2) the Secretary determines that the circumstances resulting in such ineffectiveness or termination were inadvertent, (3) no later than a reasonable period of time after discovery of the circumstances resulting in the termination, steps were taken - (A) so that the corporation is a small business corporation, or (B) to acquire the required shareholder consents, and (4) the corporation, and each person who was a shareholder of the corporation at any time during the period specified pursuant to this subsection, agrees to make such

adjustments (consistent with the treatment of the corporation as an S corporation) as may be required by the Secretary with respect to such period, then, notwithstanding the circumstances resulting in such termination, such corporation shall be treated as an S corporation during the period specified by the Secretary.

CONCLUSION

Based solely on the facts submitted and representations made, we conclude that X's election to be treated as an S corporation terminated on Date 2, when X issued stock to ineligible shareholders, Y and Z. We further conclude that the termination constituted an inadvertent termination within the meaning of § 1362(f).

X will be treated as continuing to be an S corporation on and after Date 2, provided that X's S corporation election is not otherwise terminated under § 1362(d). Z will be treated as a shareholder from Date 2 until Date 3, when the principals of Z became the shareholders of X.

This ruling is conditioned upon the shareholders of X including in income their pro rata share of the separately stated and nonseparately computed items of X as provided in § 1366, making any adjustments to basis as provided in § 1367, and taking into account any distributions made by X as provided in § 1368. If X or its shareholders fail to treat themselves as described above, this letter ruling shall be null and void.

As an adjustment under § 1362(f)(4), a payment of \$n and a copy of this letter must be sent to the following address: Internal Revenue Service, Cincinnati Service Center, 201 West Rivercenter Blvd., Covington, KY 41001, Stop 31, Terri Lackey, Manual Deposit. This payment must be sent no later than Date 4.

Except as specifically set forth above, no opinion is expressed or implied concerning the federal tax consequences of the above-described facts under any other provision of the Code, including whether X was otherwise a valid S corporation.

This ruling is directed only to the taxpayer who requested it. Section 6110(k)(3) of the Code provides that it may not be used or cited as precedent.

Pursuant to the power of attorney on file with this office, a copy of this letter will be sent to X's authorized representative.

Sincerely,

Faith P. Colson
Senior Counsel, Branch 1
Office of the Associate Chief Counsel
(Passthroughs & Special Industries)

cc: